No. 83-751

IN THE

Supreme Court of the United States

October Term, 1983

SECURITIES AND EXCHANGE COMMISSION, ET AL.,
Petitioners,

v.

JERRY T. O'BRIEN, INC., ET AL.,
Respondents

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

BRIEF OF RESPONDENTS
JERRY T. O'BRIEN, INC., JERRY T. O'BRIEN,
PENNALUNA & COMPANY, INC.,
AND BENJAMIN A. HARRISON

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(Corrected Copy)

QUESTIONS PRESENTED

Whether the respondents, who are targets of an SEC investigation, should be given notice of administrative subpoenas issued to third parties.

PARTIES TO THE PROCEEDING

Respondent Jerry T. O'Brien, Inc., is a securities broker-dealer with offices in Wallace, Kellogg, and Coeur d'Alene, Idaho, and Spokane, Washington. Its principal shareholder and chief officer is respondent Jerry T. O'Brien. (Hereafter these respondents shall be referred to as "O'Brien".)

Respondent Benjamin A. Harrison is sole shareholder of respondent Pennaluna & Company, Inc., a private investment company of Mr. Harrison. Prior to June, 1970, Pennaluna & Company, Inc., was a securities broker-dealer; it now licenses its name to respondent O'Brien. Mr. Harrison is an employee of Jerry T. O'Brien, Inc., and is also secretary of the Spokane Stock Exchange, a national securities exchange. (Hereafter these respondents shall be referred to as "Harrison".)

Co-respondent H. F. Magnuson & Company is the accountant for Jerry T. O'Brien, Inc., and for Pennaluna & Company, Inc. Co-respondent H. F. Magnuson is also a customer of Jerry T. O'Brien, Inc. (Hereafter these respondents shall be referred to as "Magnuson" or as "co-respondents".)

Respondents Jerry T. O'Brien, Inc., and Pennaluna & Company, Inc., have no parent, subsidiary, or affiliate corporations.

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STATEMENT

A. **Complaint of Respondents.**

Respondents are targets of an SEC investigation. Respondents Harrison and Pennaluna are specifically named in a Commission formal order of investigation S-1555 dated September 3, 1980. (RI, Ex. A) The formal order also names Magnuson and unspecified "others" as subjects of investigation. Respondent O'Brien is not named in the formal order. In February, 1981, after receipt of an SEC subpoena, O'Brien asserts that it was informed by SEC staff that it was not at that time a target of investigation. (R2.) In August, 1981, after complying with four SEC subpoenas, O'Brien was informed by SEC staff that it was a target; specificially, that it was one of the "others" referred to in the formal order. (R2, Ex. R.)

Respondents brought this action in September, 1981, seeking injunctive relief against investigatory conduct of the

SEC and its staff. Respondents allege that the agency's conduct has exceeded and abused statutory authority. Respondents also brought this action against co-respondent Magnuson, seeking to restrain its compliance with a subpoena issued to it pending court consideration of their claims. (Rl.)

Respondents allege that the SEC is investigating O'Brien without prior determination by the Commission, in violation of statute and its own rules.[1] Respondents allege that the SEC deceived O'Brien into complying with four subpoenas by intentionally misleading it as to its status as a target.[2]

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1. O'Brien is not named in the Commission's formal order of investigation S-1555. (Rl,Ex. A.) In February 1981, O'Brien was informed he was not a target. (R2.) In August 1981, SEC staff informed O'Brien that he was being investigated for violations of Sections 9(a)(2) and 15(b)(6) of the Exchange Act, which are not specified in the Commission's formal order. (R2, Ex. R.) The formal order describes no extraordinary events tending to show violations by O'Brien. *United States v. Bisceglia*, 420 U.S. 141 (1975). Sections 20(a) and 19(b) of the Securities Act and Section 21(a) of the Exchange Act grant authority to the Commission to initiate investigations and to delegate subpoena power to designated staff. SEC Rule 202.5, 17 C.F.R.§ 202.5, applicable at material times, required investigation of O'Brien only after a Commission determination of "likelihood" that a violation has been or is about to be committed. Any agency must scrupulously observe its own rules. *United States ex. rel. Accardi v. Shaughnessy*, 347 U.S. 260 (1954). Although the existing formal order refers to identified targets and "others", the term "others" is used by the SEC to refer to a target's officers, directors, and employees. SEC 1981 Enforcement Training Manual, p. 1-28. Congress intended a Commission decision to investigate: "Should the staff uncover information indicating the advisability of pursuing possible violations not embodied within the [existing] scope of the formal order, it must return to the Commission and seek an amendment to the order." H.R. Rep. No. 1321, 96th Cong. 2d Sess. 2 (1980) *reprinted* 4 U.S. Code Cong. and Admin. News 3877 n.2. The staff has not brought the matter of possible violations by O'Brien to the Commission's attention, and the Commission has given no approval to issuance of subpoenas for purpose of investigating O'Brien. *See* Pet. Brief p. 13 n.14, *citing* H.R. Rep. 96-1321 (Pt. 1), 96th Cong. 2d Sess. 4 n.2 (1980). O'Brien is entitled to a decision by the Commission itself. *SEC v. Wheeling Pittsburgh Steel Corp.*, 648 F.2d 118, 130 (3d Cir. 1981).

2. *See SEC v. ESM Government Securities, Inc.*, 645 F.2d 310 (5th Cir. 1981).

Respondents allege that the SEC intentionally has provided nonpublic information about the formal order and subject matter of investigation to the news media in order to harass and injure respondents.[3] Respondents allege that the SEC has issued to them, and to third parties, subpoenas which demand disclosure of information irrelevant to any legitimate purpose.[4]

B. **Respondents' Motion for Discovery; SEC's Motion to Dismiss.**

On filing of their complaint, respondents also filed a motion for discovery supported by affidavits. Respondents argued that they had shown some evidence to support their allegations which inferred a reasonable possibility of SEC misconduct exceeding or abusing authority. Respondents indicated to the court that, since evidence necessary to prove their allegations was exclusively in the hands of the SEC and its agents, respondents needed discovery in order to prove their allegations. Respondents requested discovery, by analogy to the limited discovery ordered by courts in subpoena enforcement actions. (R30; R50, p. 22-25.)[5]

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3. *See Silver King Mines, Inc., v. Cohen*, 261 F. Supp. 666 (D.C. Utah 1966); *Lynn v. Biderman*, 536 F.2d 820 (9th Cir. 1976), *cert. den.* 429 U.S. 920.

4. *See United States v. Bisceglia, supra*, 420 U.S. at 146-147 and footnote 11, *infra*.

5. See cases cited in footnote 23, *infra*. Petitioner's quotation of respondent's counsel at footnote 5 of its Brief (Pet. Brief p. 4) must be placed in this context. Few plaintiffs can prove any case without discovery. For example, the July newspaper article revealing specific details of the formal order and subject matter of investigation inferred a strong possibility of SEC misconduct. Since the reporter refused to reveal his source (Tr. 51), the SEC was the only source of evidence which would prove wrongdoing. Discovery has occurred in respondents' damage action against the SEC. Discovery has revealed that an SEC agent provided the investigatory information to a public relations employee of a corporation in a tender offer battle with respondent Magnuson, and encouraged the employee to reveal it to news media. (*See* Deposition of David Bond, May 11, 1983, p. 50.)

The SEC responded with a motion to dismiss. The SEC argued that dismissal of respondents' equitable claims was required under *Reisman v. Caplin*, 375 U.S. 440 (1964). The SEC asserted that respondents could raise their claims in a subpoena enforcement action, which under *Reisman* was an adequate remedy at law. (R42, p.11-14.) Respondents asserted that the *Reisman* remedy at law was not adequate because the SEC or its staff might issue unlawful subpoenas to third parties of whom respondents were unaware. If respondents were unaware of the third-party subpoenas, respondents would be unable to move to intervene in a subpoena enforcement proceeding to challenge the legitimacy of SEC conduct. (Tr. of September 28, 1981, at 63, 69-73, 77-78; Memorandum in Opposition to Dismissal, p. 8; Tr. of December 2, 1981, at 76-79.)

C. **District Court Order of January 20, 1982.**

On January 20, 1982, the District Court ordered dismissal of respondents' equitable claims. (Pet. App. 17a-24a.) The District Court stated that its "sole concern at present is whether subpoenas still outstanding, and the SEC's general investigation of the parties, is subject to pre-emptive attack as a matter of equity". (Pet. App. 24a.) The subpoenas then outstanding were those to Harrison and to co-respondent Magnuson.[6]

The District Court ordered dismissal because it determined that respondents had an adequate remedy at law under *Reisman* in their ability to raise their claims in challenge to the outstanding subpoenas in a subpoena enforcement action. The District Court held:

> "Long-held case law suggests that plaintiffs' ability to resist enforcement of whatever subpoenas are now outstanding or may become so in the future, and to put the government to its proof, is sufficient protection against process issued in bad faith." (Pet. App. 24a.)

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6. When this lawsuit was filed, there were six outstanding subpoenas to O'Brien and its employees which had been issued in August, 1981. (Tr. I, Ex. H.) During oral argument, the SEC informed the district court that it would not seek enforcement of these subpoenas. (Pet. App. 21a.)

The District Court declined, therefore, to grant limited discovery.

In deciding not to grant injunctive relief, the court examined the formal order and the face of the outstanding subpoenas; the court was satisfied they constituted a *prima facie* showing of legitimacy under *United States v. Powell*, 379 U.S. 48 (1964). (Pet. App. 19a, 21a.) However, the court specifically exempted O'Brien from such finding. (Pet. App. 19a-21a.) The District Court noted that a *prima facie* showing merely shifts the burden of proof to respondents. (Pet. App. 19a.) The court did not examine the merits of respondents' claims.[7/8] The District Court left determination on the merits to a subpoena enforcement action.

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7. The District Court stated that "the agency's failure to 'target' plaintiff O'Brien with a 'likelihood' finding casts some doubt upon the validity of subpoenas issued to him in that a critical administrative step was left unsatisfied." The Court cited *SEC v. Wheeling Pittsburgh Steel Corp.*, 648 F.2d 118, 127 (3d Cir. 1981), and *United States v. Powell*, 379 U.S. 48 (1964). The Court, however, noted that O'Brien had complied with subpoenas to him, and stated that "counsel has admitted that there would have been compliance even if O'Brien had known he had been 'targeted'". Counsel did not admit this. The transcript, which was not prepared until after the District Court had written its opinion, inidicates that counsel stated that O'Brien would have complied with the first subpoena of February 24, 1981. (Tr. of September 28, 1981, p. 46.) O'Brien admits it had no grounds at that time to contest this first subpoena (RI, Ex. B). However, if O'Brien had known it was a target of investigation, it would have contested all later subpoenas on the ground that they exceeded the scope of the formal order S-1555, as well as other grounds. Subpoenas issued in May, June, and July, 1981 demanded records of securities transactions by approximately 30 persons and companies not named in the formal order, and demanded records of transactions by all customers in the stock of 12 companies not identified in the order. (RI, Exs. D-G.) O'Brien complied with these subpoenas only because it believed it was not a target, and thus had motive to cooperate rather than litigate with the SEC. As soon as O'Brien was informed of its status as a target, O'Brien refused compliance with additional subpoenas (RI, Ex. H) on the grounds asserted in the complaint herein.

8. The District Court specifically declined to "consider the merits" of respondents' allegation that the SEC had leaked nonpublic investigatory information to the press. (Pet. App. 22a.)

D. District Court Order of March 25, 1982.

After the order of January 20, 1981, as the Court itself later noted, the SEC "waged an aggressive investigation, issuing numerous subpoenas" to third parties. (Pet. App. 10a.) However, the SEC did not initiate subpoena enforcement proceedings on the outstanding subpoenas to Harrison or co-respondent Magnuson.[9]

Respondents repetitioned the District Court for relief. Respondents asserted that, although the SEC was well aware of their challenges to the legitimacy and enforceability of SEC subpoenas, the SEC was proceeding to issue subpoenas to numerous third parties. Respondents asserted the likelihood that they would not become aware of many of the third-party subpoenas. Respondents reasserted their earlier position that they would have no opportunity under *Reisman* to assert those challenges in subpoena enforcement proceedings against third-party recipients unless respondents were made aware of the issuance of each subpoena. Respondents reasserted that they would have no adequate remedy at law unless the District Court ordered the SEC to provide notice of the issuance of a third-party subpoena. Two hearings on oral argument were held on this issue. (Trs. of March 9 and 18, 1981.)

On March 25, 1981, the District Court issued a second order. (Pet. App. 9a-16a.) The Court reiterated that its prior order was based upon the existence of an adequate remedy at law in the form of an enforcement hearing. (Pet. App. 10a.) The District Court agreed that without notice, respondents would be denied opportunity to intervene in an enforcement action to prevent disclosure of information to the SEC.

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9. A subpoena enforcement action was not initiated until April, 1982. The action was commenced in the District Court for the Western District of Washington at Seattle, even though all respondents reside and all documents are located in Spokane, Washington, or in Northern Idaho near Spokane, and even though this action was before the Eastern District in Spokane. The Western District ordered a change of venue to the Eastern District. *SEC v. Magnuson, et al.*, West. Dist. No. C-82-362, East. Dist. No. C-82-282. The matter is currently pending.

However, the court held, as the SEC argued, that respondents nevertheless had an adequate remedy in that they could seek suppression of evidence obtained unlawfully by the SEC in any subsequent civil proceeding. The court alternatively held that respondents lacked standing because the information sought did not "belong" to them.

E. Order of Ninth Circuit Court of Appeals.

The District Court, however, indicated it could not "say with certainty that this heretofore unresolved issue would not be determined otherwise on appeal". (Pet. App. 15a.) On appeal, the Ninth Circuit Court of Appeals ordered that the SEC provide respondents with notice of third-party subpoenas. (Pet. App. 1a-8a.)

SUMMARY OF ARGUMENT

Congress has granted the SEC limited authority to issue subpoenas for purposes of investigations. An SEC subpoena is coercive process and must be issued as authorized by law. An SEC subpoena issued in excess or abuse of authority is unenforceable.

Congress has placed enforcement of SEC subpoenas with the courts. If a subpoena is not obeyed, the SEC must petition the courts for enforcement. A subpoena enforcement action is an adversary proceeding in which the SEC must show proper exercise of authority and in which opponents may challenge the subpoena on any appropriate ground, including lack or abuse of authority.

A subpoena recipient's protection for SEC issuance of an unlawful subpoena is the recipient's opportunity to make appearance in a subpoena enforcement action to challenge the subpoena. In *Reisman v. Caplin*, *supra*, this Court extended this protection to the target of the investigation. This Court held that "both parties [subpoenaed] and those affected by disclosure" may challenge the subpoena. 375 U.S. at 445.

In *Reisman*, this Court held that the target's remedy for SEC issuance of an unlawful subpoena to a third party is the target's opportunity to move to intervene in the subpoena

enforcement action. Although intervention is permissive, the motion to intervene provides the target a means for court scrutiny of SEC exercise of authority. This Court held such motion to intervene to constitute the target's adequate remedy at law.

In *Reisman*, this Court recognized that a target would have no opportunity to intervene in a third-party enforcement action if the third party were to obey the subpoena without challenge. In *Cudahy Packing Co. v. Holland*, 315 U.S. 357, 363-364 (1942), this Court noted the coercive effect of an agency subpoena, with the likely consequence that a nontarget third party would comply. Therefore, in order to effectuate the target's intervention remedy, this Court provided that the target "might restrain compliance" by the third party "until compliance is ordered by a court". *Reisman, supra*, 375 U.S. 449-450.

The *Reisman* decision clearly assumes that the target of an investigation is aware of the SEC's issuance of a third-party subpoena. If the target is not aware of the third-party subpoena, the target obviously has no opportunity to move to intervene in an enforcement action. If the third-party recipient does not challenge or challenges ineffectively, for lack of motive or lack of evidence known to the target, then an unenforceable SEC subpoena issued in excess or abuse of authority nevertheless coerces disclosure affecting the target.

Therefore, respondents ask this Court to effectuate the target's intervention remedy created in *Reisman*, by providing the respondent target with notice of SEC subpoenas issued to third parties. Without such notice, the *Reisman* intervention remedy is ineffective and in substance illusory.

Notice to respondents of third-party subpoenas creates no new right or remedy. It merely effectuates an existing remedy. The SEC argues that notice will be abused and therefore should not be given. Respondents will not abuse such notice, and no contention is made that they will. The great majority of SEC investigations are civil in nature. The

secrecy required in criminal investigations by a Grand Jury is not applicable to civil investigations by the SEC, which lack the Grand Jury's checks, balances, and protections against prosecutorial excess. The SEC and the courts have adequate civil powers to deal with abuse of notice through protective orders, sanctions, and contempt.

The courts have inherent equitable power to protect citizens from unauthorized government misconduct. Congress has not precluded notice to respondents of third-party subpoenas. When Congress has chosen to legislate new remedies beyond the *Reisman* remedy, Congress has recognized the necessity of such notice in order to make the remedies adequate.

Respondents in this case make specific allegations of SEC misuse of its investigatory and subpoena authority. Respondents assert some evidence in support of their allegations. Respondents are, at the minimum, entitled to an opportunity for court scrutiny of the merits of their claims. Respondents should be granted notice on the same basis which would allow them discovery or intervention in a subpoena enforcement action. If the SEC cannot show a *prima facie* compliance with the standards of *United States v. Powell*, *supra*, or if respondents show sufficient evidence to infer possible SEC wrongdoing, then respondents should have notice of third-party subpoenas.

Without such notice, respondents' remedy under *Reisman* is ineffective and illusory. Respondents will be subjected to "officious intermeddling" in their affairs and interests, and harm to their reputations and businesses. *Oklahoma Press Publishing Co. v. Walling*, 327 U.S. 186, 213 (1946). Respondents will be without protection against SEC misconduct in excess and abuse of authority. Notice is necessary if respondents are to have the adequate remedy declared in *Reisman*.

ARGUMENT

I

PURSUANT TO *REISMAN V. CAPLIN*, A TARGET'S REMEDY FOR SEC ABUSE OF AUTHORITY IN ISSUANCE OF A THIRD-PARTY SUBPOENA IS THE TARGET'S OPPORTUNITY TO MOVE TO INTERVENE IN THE SUBPOENA ENFORCEMENT ACTION

A. An SEC Subpoena Must Be Issued As Authorized By Law.

Congress has granted the SEC limited authority to issue investigatory subpoenas. *United States v. Powell*, *supra*, 379 U.S. 48 (1964), *United States v. Sells Engineering*, _____ U.S. _____, 77 L. Ed. 2d 743 (1983). Such subpoena must be issued "[f]or the purpose" of aiding an investigation "to determine whether any person has violated, is violating, or is about to violate" securities statutes or regulations. Sections 21(a) and (b) of the Exchange Act, 15 U.S.C. §§ 78u(a) and (b). Such subpoena must demand documents and testimony deemed "relevant or material to" the investigative inquiry. Section 21(b) of the Exchange Act, 15 U.S.C. § 78u(b). Such subpoena must be "issued by a member of the Commission or an official designated by it". Section 21(b) of the Exchange Act. Furthermore, SEC subpoenas are not self-enforcing. In case of a refusal to obey a subpoena, the SEC must bring a subpoena enforcement action against the recipient in federal court. Section 21(c) of the Exchange Act.[10]

This statutory structure governing SEC investigations is analogous to that governing the IRS. *See United States v. Powell*, *supra*, 379 U.S. at 57. In *Powell*, this Court held that courts would not enforce an IRS summons unless the IRS could show use of the summons in accordance with statutory authority. Specifically, this Court held:

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10. *See also* Sections 20(a), 19(b), and 22(b) of the Securities Act, 15 U.S.C. 77t(a), 77s(b), and 77v(b).

> "Reading the statutes as we do, the Commissioner . . . must show [1] that the investigation will be conducted pursuant to a legitimate purpose, [2] that the inquiry may be relevant to the purpose, [3] that the information sought is not already within the Commissioner's possession, and [4] that the administrative steps required by the Code have been followed . . ."

379 U.S. 57-58.

In *Powell*, this Court reiterated its holding of eleven months earlier in *Reisman v. Caplin*, *supra*, that a subpoena enforcement action is an adversary proceeding in which opponents "may challenge the subpoena on any appropriate ground". *Powell*, *supra*, 379 U.S. at 58; *Reisman*, *supra*, 375 U.S. at 446, 449. Appropriate grounds include a challenge to the agency's compliance with the foregoing *Powell* standards; for example, the opponent might show "the summons had been *issued* for an improper purpose, such as to harass the taxpayer or to put pressure on him to settle a collateral dispute, or for any other reason reflecting on the good faith of the particular investigation." (Emphasis added.) *Powell*, *supra*, 379 U.S. at 58.

More recently, in *United States v. LaSalle*, 437 U.S. 298 (1978), this Court reaffirmed "the *Powell* standards, of [governmental] good faith". *LaSalle*, 437 U.S. at 318. This Court held that the purpose of the summons enforcement action "is to determine whether the agency is honestly pursuing the goals of [statute] by *issuing* the summons". [Emphasis added.] 437 U.S. at 316. This Court noted that the *Powell* elements were not intended as an exclusive statement, but were examples of agency action not in good-faith pursuit of congressionally authorized purposes. 437 U.S. 317 n.19.

In *LaSalle*, this Court indicated that the *Powell* standards are based upon the need to prevent both "agency abuse of congressional authority and judicial process". 437 U.S. 318 n.20. The Administrative Procedure Act specifically provides that "[p]rocess . . . or other investigative act or demand may not be *issued*, made, or enforced except as authorized by

law". (Emphasis added.) 5 U.S.C. 555(c).[11]

B. An SEC Third-Party Subpoena Is Subject To Challenge By The Target Of Investigation.

In *Reisman v. Caplin*, this Court held that "both parties summoned and those affected by a disclosure may . . . challenge the summons" issued by the IRS. 375 U.S. at 445. In *Reisman*, the attorneys for taxpayers under investigation brought suit against the IRS to challenge a summons issued to accountants engaged for the taxpayers. This Court clearly regarded the target-taxpayers as affected parties. 375 U.S. at 449-450.

In *Reisman*, this Court ruled that taxpayers and other affected parties had an adequate remedy at law in the statutory summons enforcement proceeding, and therefore dismissed their request for a declaration that the summons was void. This Court stated that the taxpayers "may intervene" in an enforcement proceeding. 375 U.S. at 449. This Court stated that, should a summons recipient indicate a willingness to comply, "either the taxpayer or any affected party might restrain compliance" pending an enforcement proceeding. 375 U.S. at 449-450.

C. An SEC Third-Party Subpoena Is Subject To Challenge By A Target On Grounds That Its Issuance Violates *Powell* Standards.

In *Reisman*, the Court indicated that appropriate grounds for challenge of an IRS summons by a recipient or affected party "would include . . . [the ground] that the material is sought for improper purpose of obtaining evidence for use

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11. "Once a summons is challenged it must be scrutinized by a court to determine whether it [complies with *Powell* standards]. The cases show that the federal courts have taken seriously their obligation to apply this standard to fit particular situations, either by refusing enforcement or narrowing the scope of the summons. *See, e.g., United States v. Matras*, 487 F.2d 1271 (CA8 1973); *United States v. Theodore*, 479 F.2d 749, 755 (CA4 1973); *United States v. Pritchard*, 438 F.2d 969 CA5 1971); *United States v. Dauphin Deposit Trust*, 385 F.2d 129 (CA3 1967). Indeed, the District Judge in this case viewed the demands of the summons as too broad and carefully narrowed them." *United States v. Bisceglia*, 420 U.S. 141, 146-147 (1975).

in a criminal prosecution". 375 U.S. at 449. Such improper purpose is a violation of *Powell* standards, namely, the conducting of an investigation for an "illegitimate purpose". *Powell, supra*, 379 U.S. 57-58. In *Donaldson v. United States*, 400 U.S. 517 (1971), this Court reiterated that the foregoing ground constitutes one of the "instances where intervention is appropriate" by a target or other affected party. 400 U.S. at 530. The issuance of a summons or subpoena for an illegitimate purpose constitutes SEC abuse of authority. *LaSalle, supra.*

In *Reisman*, the IRS issued a summons to accountants engaged by the target-taxpayer's attorney. The attorney, acting for the taxpayer, challenged the summons on grounds that it was issued for an improper purpose and that it sought documents subject to attorney-client and work-product privileges. This Court did *not* rule that the taxpayer had no right, or no standing, to challenge the third-party summons on these grounds. To the contrary, this Court specifically held that "both parties summoned and those affected by disclosure may . . . challenge the summons" on these appropriate grounds. 375 U.S. at 445.

In *Reisman*, the target-taxpayers sought to challenge the third-party summons by means of an action for declaratory and injunctive relief. This Court denied the requested relief. However, this Court did *not* rule that the taxpayers had no remedy for IRS issuance of a third-party summons in excess or abuse of authority. To the contrary, this Court held that the statutory summons enforcement proceeding provided the target-taxpayers, as well as the summons recipient, with an adequate remedy at law. This Court found the statutory remedy to be adequate because of the taxpayers' ability to challenge the summons by motion to intervene in the enforcement proceeding.

In *Donaldson*, a taxpayer acting pursuant to *Reisman* obtained injunctions restraining his employer and the employer's accountant from complying with IRS summonses. When the IRS brought an enforcement proceeding, the taxpayer moved to intervene to challenge the summons on the ground that, since the IRS had assigned

a special agent from its criminal division to the investigation, the IRS was abusing its summons authority by seeking material for the improper purpose of obtaining evidence for a criminal prosecution.

In *Donaldson*, this Court first held that intervention was permissive, and not a matter of right. Intervention was to be granted "when circumstances are proper" upon the "usual process of balancing opposing equities". 400 U.S. at 530. In *Donaldson*, this Court denied intervention on the circumstances of that case, holding that the mere assignment of a special agent did not show an improper purpose.

In *Donaldson*, this Court did not rule that the taxpayer-target had no remedy for IRS issuance of a summons in excess or abuse of its authority. Although the taxpayer target was denied intervention, he nevertheless obtained a hearing on the merits on his allegation of IRS abuse of authority.

D. An SEC Third-Party Subpoena Issued In Excess Or Abuse Of Authority Violates A Target's Interests.

As indicated previously, this Court in *Reisman* held the target of investigation to be a party affected by a third-party subpoena issued in excess or abuse of authority. It is the target's affairs that are under inquiry by the SEC; and, even though a subpoena is issued to a third party, the subpoena demands information about the target's affairs and interests.

Prior to *Reisman*, this Court recognized that Congress granted limited investigatory authority to agencies both "to secure the public interest and at the same time to guard the private ones". *Oklahoma Press Publishing Co. v. Walling*, 327 U.S. 186, 213 (1946). The statutory limits on SEC authority constitute statutory protections against "officious intermeddling, whether because irrelevant to any lawful purpose or because unauthorized by law". *Oklahoma Press*, *supra*, 327 U.S. at 213. It is the target's affairs and interests that are under investigation, and it is thus the target who needs the statutory protections against unlawful and abusive inquiry into its affairs and interests.

In *Oklahoma Press*, this Court made it clear that the affairs

and interests protected by statute "are not identical with those protected by actual search and seizure, nor are the threatened abuses the same". 327 U.S. at 213. The Fourth Amendment protects from unreasonable disclosure only documents in the possession of the target. The statutory limits on SEC authority more broadly protect the target from officious intermeddling by the SEC into the target's affairs and interests; and, therefore, the statutory limits protect from disclosure documents about a target's affairs and interests in the possession of the target of third parties. If the SEC subpoena for documents exceeds or abuses statutory authority, the possession of the documents is irrelevant.[12]

In addition, the effects on a person being subjected to an investigation are significant. There is the strong suspicion of wrongdoing. The Securities Act authorizes investigations only when "it shall appear to the Commission . . . that . . . provisions . . . have been are about to be violated". Securities Act § 20(a), 15 U.S.C. § 77t(a). The Commission's Rules of Practice, applicable when the investigation in this case was commenced, provided that the Commission may order an investigation only if there is a "likelihood that a [violation of securities laws] has been or is about to be committed". 17 C.F.R. § 202.5(a).

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12. "In the instant case, however, appellants' standing to challenge administrative summonses derives not from the Fourth Amendment, but rather from a federal statute, § 7602, and from the gloss placed upon that statute by the federal courts. . . . [T]he courts from *Reisman* and *Donaldson* onward, up to and including *LaSalle*, have identified a protectable interest in the taxpayer not to be the target of an exclusively criminal investigation in which government agents have acted beyond their statutory authority. If the civil limitation placed upon § 7602 summonses is not for the taxpayer's benefit, we have difficulty in discerning the party for whose protection it was designed. While the third-party recipients of summonses may well be motivated to refuse to comply on the grounds that the summonses are overbroad or unreasonably burdensome, there is little reason to expect them to raise the defense that the summonses were issued to further a solely criminal investigation of the taxpayer. This is not a matter of the third-party bank's interest, but of the taxpayer's." (Citations omitted.) *United States v. Genser*, 582 F.2d 292, 305-306 (3d Cir. 1978).

Common experience tells us that the accusation, or mere suspicion, of wrongdoing by a targeted person can disrupt and interfere with the business and personal relations of the targeted person with friends, associates, and other third parties who gain knowledge of the existence of an investigation. Although it may be hard to quantify, the harm to the target is immediate and real.[13] A person should not be subjected to an investigation unless that investigation is lawful. If the investigation is legitimate, then such harm must be accepted. However, a target must have the opportunity to demand that an agency justify its conduct by the showing of legitimacy required by *Powell* and *LaSalle*.

The limits on an agency's statutory authority constitute the standards for enforcement of agency subpoenas set forth in the *Powell* decision. The SEC has no right to inquire, by means of any subpoena to anyone, into a target's affairs and interests in excess or abuse of statutory authority. Correspondingly, in the words of the Ninth Circuit opinion below, respondents, "as target's of investigation, do have a right to be investigated consistently with *Powell* standards". (Pet. App. 6a.)

E. A Target's Remedy For SEC Issuance Of An Unauthorized Third-Party Subpoena Is Opportunity To Move To Intervene In The Subpoena Enforcement Action.

Under *Reisman* the target of an SEC investigation has a right to challenge a subpoena to a third party on any appropriate ground. Appropriate grounds for challenge constitute appropriate grounds for intervention. *Reisman, supra*; *Donaldson, supra*. Such appropriate grounds include the SEC's failure to meet the *Powell* standards of governmental good faith. *Reisman, supra*; *Powell, supra*; *Donaldson, supra*. The target *must* challenge the third-party subpoena by motion to intervene in a subpoena enforcement proceeding, since opportunity to intervene in such proceeding

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13. There is great "potential for damage to a citizen's reputation when the government starts to ask someone else questions about that citizen". *Saunders v. Schweiker*, 508 F. Supp. 305, 309 (D.C.N.Y. 1981).

constitutes a target's adequate remedy at law for SEC violation of *Powell* standards.

In order to assure a target's opportunity for intervention, the courts will enjoin the third-party recipient from obeying the subpoena pending an enforcement proceeding. *Reisman*, *supra*. Although a target's intervention in such proceeding is permissive, the target is at least entitled to court review of its motion to intervene and the grounds therefor, and upon a balancing of the equities may be entitled to intervention. *Donaldson*, *supra*.

II

THE TARGET MUST HAVE NOTICE OF THE ISSUANCE OF A THIRD-PARTY SUBPOENA IF THE TARGET'S *REISMAN* REMEDY IS TO BE EFFECTIVE

A. A Target's Remedy For SEC Issuance Of An Unauthorized Third-Party Subpoena Necessitates Notice

Obviously, the foregoing *Reisman* intervention remedy presupposes that the target "is aware of the issuance of the [third-party subpoena] prior to compliance". *United States v. Genser*, 582 F.2d 292, 300-301 (3d Cir. 1978). If the target has no notice of the third-party subpoena, then the *Reisman* decision is a nullity because the target has no opportunity to "challenge the [subpoena] on any appropriate ground". *Reisman*, 375 U.S. at 449. Without notice, the target has no adequate remedy at law in opportunity to intervene in a subpoena enforcement proceeding.

In *Reisman*, this Court recognized that a target would have no opportunity to intervene in an enforcement action if the third party were to obey the subpoena without challenge. A third party does not share the same interests as a target to challenge a subpoena. A third party, who is told or believes he or she is not a target, suffers only the inconvenience of producing documents or giving testimony as requested, and no other adverse effects. The third party does not have the

conviction of principle, or other motivation, to undertake the costs inherent in litigating with the government.[14]

This Court has itself noted with respect to agency subpoenas:

> "True, there can be no penalty incurred for contempt before there is a judicial order of enforcement. But the subpoena is in form an official command, and even though improvidently issued it has some coercive tendency, either because of ignorance of their rights on the part of those whom it purports to command or their natural respect for what appears to be an official command, or because of their reluctance to test the subpoena's validity by litigation." *Cudahy Packing Co. v. Holland*, 315 U.S. 357, 363-64 (1942), *quoted* in *United States v. Minker*, 350 U.S. 179, 187 (1956).

If the SEC issues a subpoena to a target, the target has motivation to refuse compliance. If the target does so, the agency will be forced to initiate a subpoena enforcement action in the courts. And the courts will require the agency to show legitimate purpose, relevancy, and the other requisites of *Powell* prior to enforcement. The courts will allow the target to challenge the authority of the SEC. A subpoena in excess of or in abuse of authority will not be enforced.

On the other hand, if an investigating agency issues a subpoena to a third party, the third party will likely have no motive not to comply. Additionally, a third party may not know that the agency subpoena is not enforceable unless so ordered by a court. Indeed, the form of subpoena used by the SEC in this case (at least the ones respondents know about), and the letters accompanying such forms, *do not* inform the persons and entities subpoenaed that they can resist compliance and contest the subpoena in an enforcement action. (See Exhibits to Rl, and also Exhibits to R102.)

In short, an agency which issues subpoenas to third parties rather than targets will likely avoid court scrutiny of the legitimacy of its investigative conduct. The agency can,

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14. See footnote 19, *infra*.

therefore, consciously avoid such showing. A questionable investigation will go forward, and an otherwise unenforceable subpoena will coerce disclosures. The agency will thus exceed or abuse its statutory authority and the process of the courts.

The *Reisman* decision clearly assumes that the target of an investigation is aware of the SEC's issuance of third-party subpoenas. If the target is not aware of the third-party subpoena, the target obviously has no opportunity to move to intervene in an enforcement action.

In order to effectuate the target's intervention remedy, this court in *Reisman* provided that the target might restrain compliance by the third-party recipient of a subpoena until compliance is ordered by a court. Respondents ask that the intervention remedy created in *Reisman* be further effectuated by providing the target respondents with notice of SEC subpoenas issued to third parties. Without such notice, the *Reisman* intervention remedy is ineffective and in substance illusory.

B. A Target Has No Remedy In Suppression Of Evidence.

The SEC argued in this case before the courts below that notice to respondents of third-party subpoenas was unnecessary because targets were afforded adequate remedy in a motion to suppress at trial, be it criminal or civil. (Tr. of March 9, 1981, pp. 28, 31-32; Tr. of March 18, 1981, p. 9; Pet. App. 11.) The SEC based this argument on language in *Donaldson*, and upon several lower court decisions construing the *Donaldson* language.[15] The District Court agreed with the SEC. (Pet. App. 13a.)

Donaldson did not create a civil suppression remedy. The Court considered only "Donaldson's particular situation".

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15. *See United States v. Genser, supra*, 582 F.2d 292 (3d Cir. 1978); *United States v. Friedman*, 532 F.2d 929 (3d Cir. 1976); *SEC v. Laird*, 598 F.2d 1162 (9th Cir. 1979). The SEC in other cases has argued against a suppression remedy. *See SEC v. ESM Government Securities, Inc., supra*, 645 F.2d 310 (5th Cir. 1981).

400 U.S. at 530. The summons involved was for routine business records of Donaldson's employer. The summons met all *Powell* standards, and was enforceable, for *civil* purposes. Donaldson challenged the summons on the sole ground that the IRS was seeking the records for the improper purpose of use in a *criminal* prosecution. The Court stated that intervention was unnecessary *in his case* because, to the extent he had any protectable interest, he could assert it and seek suppression in any subsequent *criminal* trial.

In the case at hand, respondents challenge the SEC subpoenas on civil, not criminal, grounds. Respondents have no right to suppression or exclusion in any subsequent civil trial or administrative hearing. *See United States v. Janis*, 428 U.S. 433 (1976). No court, to respondents' knowledge, has ever granted civil suppression of documents or testimony obtained by abuse of congressional authority or judicial process. If such abuse is to be remedied, the court must "prevent the wrong before it occurs". *United States v. Calandra*, 414 U.S. 338, 346 (1974).

C. The SEC Is Not A Grand Jury And Has No Inherent Right To Investigate Without Notice

The SEC argues that the consequences of providing notice to targets will be a "parade of horribles". If given notice, targets might flee prosecution, destroy documents, fabricate testimony and intimidate witnesses. The SEC argues that to prevent these possibilities, it must be granted the authority to operate in secret, like a grand jury.

The SEC's argument does not follow. First, the great majority of SEC investigations are for civil violations.[16] Although there may be reason to presume that persons

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16. The *SEC 48th Annual Report 1982* indicates that the SEC's "principal enforcement remedy is a Federal court injunction". *Report*, p. 1. The Report indicates that in 1982 it initiated 145 injunctive actions and 106 administrative proceedings. In 1982, it procured 136 injunctions involving 418 defendants, and in administrative proceedings revoked registrations, barred, suspended or censured 193 defendants. In 1982, the SEC was involved in procuring 24 criminal indictments against 47 defendants.

suspected of criminal conduct may possibly flee or obstruct an investigation, there is no reason to presume persons suspected of civil violations will do so. A civil investigation is no different in this respect from civil discovery in normal civil lawsuits under the Rules of Civil Procedure. Under those rules, a court has power to deal with abuses through protective orders, sanctions, and contempt. Abuses of notice to targets can be adequately dealt with by analogy to civil procedure; analogy to criminal Grand Jury procedure is not justified.[17]

Second, Grand Jury secrecy is justified on two bases: (1) the prevention of obstruction by targets, and (2) the protection of citizens against unfounded prosecutions. *Sells Engineering, supra*; *SEC v. ESM Government Securities, Inc.*, 645 F.2d 310, at 312-13 (5th Cir. 1981). In order to protect citizens against prosecutorial overreaching, the Grand Jury operates "independently" of the prosecutor as a check and balance on possible prosecutorial abuse. *Sells Engineering, supra.* In contrast, the SEC operates to both investigate and prosecute. The only check and balance on SEC abuse of authority is the statutory subpoena enforcement action and intervention therein under *Reisman.* This check and balance is illusory and ineffective without notice of third-party subpoenas to the target of investigation.

Third, Congress has specifically required that the Grand Jury exercise its inherent powers in secret. Federal Rule of Criminal Procedure 6(e). The SEC's authority to investigate is not inherent, but is a creature of statute. Congress has neither specifically required nor authorized the SEC to investigate in secret. And, indeed, the SEC claims discretion to investigate publicly, secretly without notice, or anywhere in between.

If the SEC can conduct secret civil investigations, without notice to targets of either the investigation or third-party subpoenas, then the SEC is more powerful than the Grand

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17. Please refer to Respondents' Brief In Opposition To Petition For A Writ Of Certiorari, pp. 25-37.

Jury. The SEC would be allowed without check or balance to secretly investigate citizens for civil violations and to use the product of secret subpoenas to prosecute civil actions against those citizens. This cannot be the intent of Congress or this Court. *Sells Engineering, supra.*

SEC investigations are not analogous to the Grand Jury for all purposes. *Hannah v. Larche*, 363 U.S. 420 (1960). In *Oklahoma Press Publishing Co., supra*, this Court recognized that agency investigations are also analogous to civil discovery. 327 U.S at 216. Civil discovery is the proper analogy for purposes of notice to targets of third-party subpoenas. Any presumption that citizens under civil investigation will obstruct justice is wholly unjustified.[18]

As Professor Bloomenthal has commented:

> "In an effort to rationalize its position, the Commission [SEC] has expressed concern that premature disclosure 'might allow prospective witnesses . . . to fabricate stories to correspond with testimony that has already been given by others'. It is submitted that such a position disregards laws pertaining to perjury and suborning perjury; is an affront to all members of the bar and disregards now longstanding experience with discovery in the courts."
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> H. Bloomenthal, Vol. 3, *Securities Law Series, Securities and Federal Corporate Law*, § 1.12[4] at 1-50.14, *quoting* James W. Ruddy, *Freedom of Information Act*, Release No. 34 (Oct. 20, 1975), 8 S.E.C. Doc. 193 (Nov. 5, 1975).

D. Congress Has Not Precluded Notice to Targets.

The SEC argues that Congress has not required that such notice be given to targets of SEC investigations. On

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18. The SEC asks, "Who is a target?" In the case at hand, there is no question that respondents are targets. A target is any identified person, individual or corporate, whose conduct the SEC suspects may violate securities laws. The SEC may investigate events, as in *United States v. Bisceglia, supra*, 420 U.S. 141, without knowing the identity of some or all the persons causally related to those events. But once it knows the identity of any suspected persons, that person is a target. If the SEC subpoenas information from a third party about another person, that person is a "party affected by disclosure" under *Reisman*.

the other hand, Congress has not required that SEC investigations be conducted in secrecy without notice. With the exception of specific situations, Congress has been silent with respect to the general issues of notice and secrecy in SEC investigations. In those situations where Congress has expressly provided that targets be given notice of third-party subpoenas, Congress has done so to effectuate a newly created right or remedy which goes beyond the *Reisman* remedy.

Under Internal Revenue Code Sec. 7609, which deals with IRS summons to banks, securities brokers, accountants, and other "record keepers" for a target-taxpayer, (1) Congress has granted the target a *right* to intervene in the summons enforcement action (Sec. 7609(b)(1)); (2) in addition, Congress has granted the target a *right* to initiate a proceeding to quash the summons (Sec. 7609(b)(2)(A)); and (3) Congress has provided that the IRS shall not examine documents summoned until the target has opportunity to exercise the foregoing rights (Sec. 7609(d)). In contrast, under *Reisman*, (1) the target's intervention remedy is permissive, not a matter of right; (2) the target has no right to *quash* since opportunity to intervene is an adequate remedy at law; and (3) the agency may examine the documents unless the target initiates action to procure or restrain the third party's noncompliance.

The target's rights under IRC Sec. 7609 go far beyond the *Reisman* remedy. Congress recognized that these newly created rights can be effectively asserted only if the target has notice of the third-party summons. Moreover, Congress acknowledged the target's permissive opportunity to intervene, and expressly provided that notwithstanding this rule of law, the taxpayer-target would have a *right* to intervene in enforcement proceedings against record keepers (Sec. 7609(a) and (b)(1)).[19]

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19. *See* H.R. Rep. 94-658, 94th Cong. 2d Sess. 307 (1976) *reprinted* 4 U.S. Code Cong. and Admin News 3203 (1976).

Congress has shown no intention to render *Reisman* ineffective, and therefore has shown no intention that notice should not be required to effectuate *Reisman*. Indeed, the congressional scheme under IRC Sec. 7609 provides a legislative model for the need for notice under *Reisman*.

Similarly, under the Right to Financial Privacy Act (RFPA), 12 U.S.C. § 3401, *et seq.*, which deals with a summons or subpoena to the bank or "financial institution" of any target, (1) Congress has granted the target a *right* to commence a proceeding to quash the subpoena in lieu of all other remedies (12 U.S.C. § 3405); (2) Congress has provided that the third party cannot comply with the subpoena, and the SEC cannot obtain documents, until the target has opportunity to quash (12 U.S.C. §§ 3402 and 3403; and (3) Congress has limited the SEC's use of subpoenaed information (12 U.S.C. § 3413). [20]

Footnote (con't)

"The use of the administrative summons, including the third-party summons, is a necessary tool for the IRS in conducting many legitimate investigations concerning the proper determination of tax. . . . On the other hand, the use of this important investigative tool should not unreasonably infringe on the civil rights of taxpayers, including the right to privacy. . .

"The committee believes that many of the problems in this area would be cured if the parties to whom the records pertain were advised of the service of a third-party summons, and were afforded a reasonable and speedy means to challenge the summons where appropriate. While the third-party witness also has the right of challenge, even under present law, the interest of the third-party witness in protecting the privacy of the records in question is frequently far less intense than that of the person to whom the records pertain."

The report goes on to state that the purpose of notice is to give the affected party "opportunity . . . to raise defenses which are already available" under the existing law. H.R. Rep. 309, 4 U.S. Code Cong. and Admin. News 3205. *See also* Sen. Rep. 94-938, 94th Cong., 2d Sess. 368-371.

20. *See* H.R. Rep. No. 95-1383, Sen. Rep. No. 95-1273, 95th Cong. 2d Sess. 219 (1978) *reprinted* 7 U.S. Code Cong. and Admin. News 9349: "The Government may obtain financial records using an administrative sub-

These protective rights are in lieu of, and go far beyond, the *Reisman* intervention remedy.

Again, Congress recognized that the effectiveness of the congressionally created RFPA remedy necessitates notice to the target of the third-party subpoena (12 U.S.C. § 3405). The judicially created *Reisman* intervention remedy likewise necessitates such notice. Unless notice is provided, a target's opportunity to intervene is dependent on the unreviewable discretion of the SEC, on the whim of a third party, and on happenstance that the target becomes aware of the subpoena in time to do something.

In *Reisman* and *Donaldson*, this Court was certainly aware that Congress by statute had made no express provision for intervention by affected parties in a subpoena enforcement proceeding, or for restraining of subpoena recipients from compliance to allow an intervention motion. This Court created the intervention remedy by using the existing statutory mechanism. This Court recognized a right in the target, or other affected party, to challenge agency exercise of its summons authority, and as a remedy the Court found a mechanism for the expression of that right. In order to fully effectuate the recognized right, these parties must have notice of the issuance of third-party subpoenas.

E. The Courts Have Power To Effectuate The *Reisman* Remedy

It is the responsibility of the courts to insure that administrative action is consistent with governing statute, and thus does not exceed or abuse authority. *Oklahoma*

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poena or summons. Authority to issue such process must be granted by some other provision of law. Such process may be used only if there is reason to believe that it will produce information relevant to a legitimate law enforcement purpose. This standard is comparable to that in existing law for testing subpoenas. . . . 'Law enforcement' is broadly defined in section 1101, but the requirement that the purpose be 'legitimate' is an important safeguard. It is intended to prevent an agency from acting outside the scope of its statutory authority, (e.g., investigating a violation over which it has no jurisdiction), as well as from pursuing an investigation in bad faith to harass or intimidate its subject."

Press, *supra*, 327 U.S. 186, 214-218; *FCC v. Schreiber*, 381 U.S. 279, 291; *SEC v. Csapo*, 533 F.2d 7, 11 (D.C. Cir. 1976). The *Reisman* intervention remedy is an example of the exercise of that responsibility. Effectuation of that remedy through notice to a target of a third-party subpoena is further exercise of that responsibility.

The SEC's issuance of a subpoena involves the process of the courts. A subpoena is issued because compulsion is necessary to coerce information a person will not voluntarily give. The coercive force of an SEC subpoena results only from the court's ability to enforce it. When the SEC issues a subpoena, it therefore invokes the process of the court. In issuing a subpoena, the SEC announces, in effect, that it can meet the *Powell* and *LaSalle* requirements. An SEC subpoena which is issued in violation of the *Powell* and *LaSalle* requirements is thus an abuse of the the court's process. The "Court may not permit its process to be abused". *Powell*, *supra*, 379 U.S. 58.

The court has inherent power in equity both to effectuate its *Reisman* remedy and to protect its process. *Hecht v. Bowles*, 321 U.S. 321 (1944); *Gumbel v. Pitkin*, 124 U.S. 131 (1888). The court's equitable jurisdiction is comprehensive and is subject to limitation only if restricted by express provision, or inescapable inference, of statute. *Weinberger v. Romero-Barcelo*, 456 U.S 305 (1982).

F. Notice To A Target Occasions No More Delay Than Is That Inherent In Existing Procedures.

Notice is necessary to effectuate a target's remedy under *Reisman* to intervene in a subpoena enforcement action Without question, a subpoena enforcement proceeding may occasion some delay of an SEC investigation. However, such delay has been imposed by Congress itself, in order to subject SEC exercise of its limited authority to judicial supervision and to allow appropriate challenges to the subpoena. *Oklahoma Press*, *supra*, 327 U.S. 216-217;

Reisman, supra; *Powell, supra*; *LaSalle, supra*. The courts have well-tested civil procedures to assure any delay is kept a minimum.[21]

The foregoing process is neither upset nor lengthened by a motion to intervene under *Reisman* on behalf of a target or other affected party. Obviously, a target who is aware of the subpoena has opportunity to contact the recipient. The target can then request noncompliance or, if necessary, under *Reisman* can restrain compliance. As a result, some third-party recipients, who absent target contact would have obeyed the subpoena, will now fail to comply. Such delay is contemplated by and inherent in the *Reisman* decision. Any delay associated with notice to targets of third-party subpoenas is likewise inherent in the *Reisman* decision.

Moreover, both the SEC itself and the courts have the discretion to establish time limitations which are reasonable under the particular circumstances. The SEC can set the return date on its subpoena, and thus limit the response time on notice to the target. If the subpoena is not complied with on the return date, the SEC can request, and the court can order, the recipient to show cause within a few days or less. The SEC can be prepared to promptly answer the motion to intervene of a target or other affected party. The court can appropriately shorten time for consideration of such motion.

Notice to a target of third-party subpoenas does not hamper the SEC's investigation with trial-like procedures. Notice does no more than effectuate a target's opportunity to participate in an adversary subpoena enforcement

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21. The SEC investigation of respondents is *not* one requiring great speed. The formal order of investigation was made in September, 1980. Prior to this, according to deposition testimony of an SEC attorney relating to respondents' nonequitable claims in this suit, an informal investigation had been conducted since mid-1978. (*See* Dep. of George Prince, April 29, 1982.) The first subpoena to O'Brien was on February 24, 1981, approximately six months after the formal order. Additional subpoenas were issued to O'Brien and Harrison over the next six months.

action. Notice does not affect the SEC's discretion to determine whom and what to investigate. Notice does not imply that a target has a right during the investigation to confront accusing witnesses or to cross-examine any witnesses.[22]

In summary, as the Ninth Circuit noted in its decision below, a subpoena enforcement proceeding is normally disposed of on affidavit alone. (Pet. App. 7a.) Few cases proceed to a limited evidentiary hearing, and only rare cases necessitate limited discovery. Notice to a target of SEC issuance of a third-party subpoena occasions no more delay to an investigation than that inherent in the statutory subpoena enforcement proceeding itself.

G. In Any Event, A Target Should Be Granted Notice Of Third-Party Subpoenas When The SEC Fails To Show *Powell* Standards Or When The Target Shows Proper Circumstances

Respondents make specific allegations that the SEC and its staff have engaged in investigative conduct, and issued subpoenas, in excess and abuse of statutory authority. Respondents have produced, and can further produce, some evidence which infers a reasonable possibility of SEC misconduct in support of their allegations. Respondents

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22. Petitioner places heavy reliance on *Hannah v. Larche*, *supra*, 363 U.S. 420. The reliance is misplaced. The respondents in *Hannah* were being investigated by a "purely investigative" agency without any authority to prosecute whatsoever. 363 U.S. 442. The respondents in *Hannah* asserted rights to be informed of specific charges, to confront accusing witnesses, and to cross-examine witnesses. Respondents in this case assert no such rights.

Unlike the agency in *Hannah*, the SEC both investigates and prosecutes. It is normal SEC practice that the same SEC attorney both investigates a person and civilly prosecutes the same person. Investigative subpoenas are used long after a decision to prosecute as a means of *ex parte* discovery for purposes of prosecution. *Hannah* constitutes no authority for denial of notice to respondents of third-party subpoenas. To the contrary, as the Ninth Circuit noted, this Court in *Hannah* acknowledged "no reason is apparent why, simply as a matter of good will, the Commission [SEC] should not in ordinary cases send a copy of its order for investigation to the person under investigation". 363 U.S. 447 n.28; Pet. App. 8a.

under these circumstances assert that they should receive notice of third-party subpoenas, and that they should have an opportunity for a hearing on the merits prior to a denial of such notice. Respondents have had no hearing on the merits of their claims.

A target's opportunity to intervene in a third-party subpoena enforcement action is permissive. A target is allowed to intervene "when circumstances are proper" upon the "usual process of balancing the opposing equities". *Donaldson, supra*, 400 U.S. at 530. Likewise, a target should be granted notice of third-party subpoenas under proper circumstances upon a balancing of the equities.

The Courts of Appeal have worked out flexible procedures to implement *Powell, Reisman, and LaSalle.*[23] In a subpoena enforcement action, the SEC must make an initial *prima facie* showing that the subpoena meets *Powell* standards. The showing is normally made in the affidavit in support of the SEC's application for an order to show cause why the subpoena should not be enforced. If the SEC fails to make such showing, the District Court will not enforce the subpoena. On the other hand, once such showing has been made, the burden shifts to the opponent to prove that the subpoena has been issued in excess or abuse of authority, or that it should not be enforced on some other ground.

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23. *See U.S. v. Fensterwald*, 553 F.2d 231 (D.C. Cir 1977); *U.S. Salter*, 432 F.2d 697 (1st Cir. 1970); *SEC v. Howatt*, 525 F.2d 226 (1st Cir. 1975); *SEC v. Knopfler*, 658 F.2d 25 (2d Cir. 1981), *cert. den.* 455 U.S. 908 (1982); *United States v. McCarty*, 514 F.2d 368 (3d Cir. 1975); *United States v. Genser*, 582 F.2d 292 (3d Cir. 1978); *SEC v. Wheeling-Pittsburgh Steel Corp.*, 648 F.2d 118 (3d Cir. 1981); *United States v. Wright Motor Co.*, 536 F.2d 1090 (5th Cir. 1976); *United States v. National State Bank*, 454 F.2d 1249 (7th Cir. 1972); *United States v. Turner*, 480 F.2d 272 (7th Cir. 1973); *United States v. Kis*, 658 F.2d 526 (7th Cir. 1981), *cert. den.*, 455 U.S. 1018 (1982); *United States v. Church of Scientology*, 520 F.2d 818 (9th Cir. 1975); *Lynn v. Biderman*, 536 F.2d 820 (9th Cir. 1976); *United States v. Samuels, Kramer & Co.*, 712 F.2d 1342 (9th Cir. 1983).

The opponent's burden is not easily met. The opponent must do more than allege an appropriate ground. The opponent must produce some evidence, through affidavit, to support its allegations. In the absence of some evidence, the subpoena will be enforced. If some evidence is shown from which the court may infer a possibility of wrongful conduct, then the court will allow a limited evidentiary hearing normally involving no more than cross-examination of the agent issuing the subpoena. The purpose of such examination is to determine whether the court will allow further limited discovery. Discovery will be allowed only where the court determines that SEC conduct is likely to be substantiated. If no discovery is warranted, the subpoena is enforced. *See United States v. Samuels, Kramer & Co., supra*, 712 F.2d 1342 (and other cases cited in footnote 23).

On a target's motion to intervene in a third-party subpoena enforcement action, a similar procedure should be followed in balancing the equities. The SEC's showing of *Powell* standards in its affidavit is before the Court. If the showing is satisfactory to the Court, the target will not be permitted to intervene (1) unless the target alleges an appropriate ground, and (2) unless the target produces some evidence sufficient to infer the possibility of SEC wrongdoing. For example, the target in *Donaldson* was not allowed to intervene for failure to meet these conditions. If the target meets these conditions, it will be allowed to intervene in the subpoena enforcement action for purposes of a limited evidentiary hearing or discovery.

On a target's application for notice of third-party subpoenas, a similar procedure should be followed in balancing the equities. The target's application must specifically allege appropriate grounds for challenge to third-party subpoenas. The SEC may answer with an affidavit showing *prima facie* that its conduct meets *Powell* standards. If such showing is not made, or if the target produces by affidavit some evidence sufficient to infer a possibility of SEC misconduct affecting the enforceability of third-party subpoenas, then the court would order notice of third-party subpoenas.

On a target's application for notice, even if the target meets the foregoing conditions, the Court in balancing the equities may nevertheless refuse to order notice if it finds a likelihood that the target would use notice of third-party subpoenas to destroy documents, intimidate witnesses, or otherwise obstruct the investigation.

At the minimum, if *Reisman* is to have practical effect, respondents are entitled to the foregoing minimal protections. No claim has ever been made in this case that respondents, if given notice of third-party subpoenas, will abuse that notice. Respondents have legitimate claims and some evidence of SEC misconduct. Respondents have a remedy under *Reisman*, but only if they have notice of third- party subpoenas.

CONCLUSION

The judgment of the Court of Appeals should be upheld. Respondents should have notice of SEC subpoenas to third parties.

Respectfully submitted,

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DATED March 22, 1984.